Testimony on Using FHA for Housing Stabilization and Homeownership Retention,

Submitted to the

House Committee on Financial Services

by the National Council of State Housing Agencies

April 10, 2008

Chairman Frank, Ranking Member Bachus, and members of the Committee, I am Doug Garver, executive director of the Ohio Housing Finance Agency. I am testifying today on behalf of the National Council of State Housing Agencies (NCSHA) in support of your economic, mortgage, and housing rescue bill.

NCSHA is grateful to you, Mr. Chairman, for this important legislation and for all you are doing to soften the impact of today's housing crisis on America's working families, communities, the housing market, and the economy. This legislation would provide states many helpful new tools in our efforts to keep families at risk of foreclosure in their homes and put foreclosed properties quickly back into productive use.

NCSHA represents the Housing Finance Agencies (HFAs) of the 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. State HFAs issue tax-exempt private activity bonds (Housing Bonds) and allocate the Low Income Housing Tax Credit (Housing Credit) to finance low-cost mortgages for lower-income first-time homebuyers and affordable apartments for low-income renters in virtually every state. HFAs administer HOME funding in 42 states to provide both affordable ownership and rental housing for low-income families.

State HFAs use Federal Housing Administration (FHA) single-family mortgage insurance in combination with our Mortgage Revenue Bond (MRB) financing programs in 44 states. HFAs used FHA insurance on 35 percent of the MRB loans we originated in 2006.

State HFAs have a long and strong track record of making mortgage loans to lower-income first-time homebuyers at rates they can afford and with underwriting standards they can meet. We have proven that you can help lower-income families achieve sustainable homeownership under more flexible terms than the conventional market offers without engaging in risky lending. HFA MRB loan portfolios are sound, with low delinquency and foreclosure rates.

While state HFAs have not contributed to the subprime mortgage problem, we want to be part of the solution by helping struggling homeowners avoid foreclosure and getting foreclosed homes off the market and into the hands of low and moderate-income buyers and renters. We are committed to doing this prudently, as no one is helped if we repeat this housing tragedy by putting people into housing situations they cannot afford to sustain.

FHA Insurance for Homeownership Retention Mortgages

Several state HFAs have taken steps over the last several months to help homeowners at serious risk of foreclosure hold onto their homes. More than a dozen HFAs, including the Ohio and Massachusetts HFAs, have established mortgage refinancing programs aimed at homeowners with subprime mortgages no lender could have reasonably expected them to be able to repay.

I testified before this Committee last year on Ohio's refinancing program. I would be pleased to share with you, Mr. Chairman, and other members of the Committee and your staff information on Ohio's and other HFAs' refinancing programs and their results to date. Other state HFAs are closely monitoring activity under these programs to inform their own refinancing program plans.

Those HFAs with subprime refinancing programs, including Ohio, have so far experienced disappointingly little volume under them. We and other HFAs have found that many troubled homeowners have one and often times many of the following obstacles in the way of refinancing their mortgages:

- They have waited too long to seek help and are so far behind on their mortgage payments that refinancing is no longer an option;

- Their incomes are too low, debt-to-income ratios too high, and/or credit scores too weak to meet even the more flexible underwriting standards state HFAs impose;

- Their outstanding mortgage obligations exceed the value of their homes, making refinancing impossible without loan restructuring or write-downs, which lenders are often reluctant to permit; and/or

- They cannot afford even the less costly mortgage loans state HFAs offer, and HFAs are constrained from offering more attractive loans terms by resource limitations, their inability to use low-cost MRB mortgage money for refinancing, and the lack of affordable mortgage insurance options.

Your legislation's FHA homeownership retention mortgage program would help lower some of these hurdles. By creating the option of an even more aggressive FHA refinancing product than FHASecure, it would encourage lenders to write down high-risk mortgages that exceed home values to avoid even greater losses upon their foreclosure. It would also allow HFAs and other lenders to offer more affordable and flexible mortgage refinancing products with the backing of FHA insurance.

We believe this FHA refinancing program would be even more successful if Congress would simultaneously authorize the use of the MRB program for subprime mortgage refinancing and increase state Housing Bond authority to accommodate this refinancing activity and increased demand among lower-income first-time homebuyers for affordable, flexible mortgage money in the wake of the subprime mortgage market collapse. House Ways and Means Committee Chairman Rangel has proposed a temporary $10 billion Housing Bond cap increase and MRB refinancing authority as part of housing stimulus legislation, the Housing Assistance Tax Act of 2008, his Committee is expected to report on April 9. Pending Senate housing stimulus legislation contains similar provisions. We urge Committee members to support these provisions and ensure they are part of whatever final housing stimulus bill Congress produces.

NCSHA also suggests the Committee consider the following modifications to the legislation's FHA refinancing program to encourage lender participation and potentially help a broader spectrum of homeowners.

Since this program is voluntary, it must provide adequate incentives for lenders to participate to have any significant impact. We are concerned that many lenders may not be sufficiently motivated to participate in the program if they receive no more than 85 percent of a property's current appraised value, especially when appraised value may be significantly less than the unpaid principal loan balance in many cases.

You may wish to consider permitting higher loan-to-value ratio mortgages to produce greater loan payoffs for current mortgage holders. We suggest that the bill at least allow FHA to insure mortgages up to the same loan-to-value ratio as permitted under its standard single-family insurance products, which is 96.5 percent.

The bill restricts program eligibility to first mortgages originated between January 1, 2005 and July 1, 2007. We recommend you expand this timeframe, as lenders in many states began originating subprime mortgages in significant numbers as early as 2001.

Many eligible loans will have second loans and liens that give other interested parties authority to reject loan payoffs. We suggest you encourage subordinate lender participation by allowing them to share in loan payoffs.

Since some HFAs are currently administering subprime refinancing programs, we recommend you permit FHA to insure program-eligible loans they have already originated.

Homeownership Counseling

Before troubled homeowners can be helped, they must be reached and educated about their options. Given their large numbers and sometimes complex circumstances, this requires substantial resources. For this reason, NCSHA strongly supports the $200 million in loss mitigation counseling funds this bill authorizes for this year and next and urges its quick appropriation.

We also applaud Congress' action last year to provide $180 million of foreclosure mitigation counseling funds through NeighborWorks, with which state HFAs successfully partner in many states. Just last month, NeighborWorks awarded $39 million of these funds to 32 state HFAs. HFAs are already using these funds to train home counselors and support local counseling efforts.

State HFAs are also active participants in HUD's Housing Counseling program. In 2007, 15 HFAs received almost $2.5 million in HUD grants.

Several HFAs, including Ohio, have invested our own funds in housing counseling. When we launched our Opportunity Loan refinancing program last year, our HFA made a $3.1 million grant from agency resources to support the NeighborWorks Foreclosure Prevention Rescue Program. This program has enabled 12 Ohio NeighborWorks organizations, including Neighborhood Housing Services in Cleveland, to offer one-time assistance to moderate-income borrowers who are experiencing temporary difficulties meeting their mortgage payments.

State HFAs are also investing significant resources in proactive marketing and outreach, with the goal of reaching troubled owners early, even before they realize they will soon confront mortgage payments they cannot afford. We have found that if we reach homeowners before they are delinquent on their mortgages, we have a much better chance of helping them. We urge you to allow the use of some counseling funds for this purpose.

State-Administered Loans and Grants for Purchase of Foreclosed Homes

Sadly, despite the best efforts of state HFAs and others to help troubled homeowners keep their homes, many will still lose them. Foreclosure rates are up significantly and still rising in many parts of the country.

Foreclosed properties are especially concentrated in lower-income neighborhoods, which were targeted by subprime lenders. These vacant properties deteriorate rapidly if not quickly resold or put into some other productive use. They destabilize these often already fragile communities by further depressing home values, discouraging investment, and contributing to vagrancy and crime.

The market will not resolve this problem on its own without unacceptable human and economic costs. New buyers simply will not be able to absorb the historic inventory of foreclosed properties we expect to see over the next several years.

State HFAs, partnering with local communities and nonprofit groups, are working aggressively to turn this foreclosed property crisis into an opportunity for low and moderate-income working families. We are looking for ways to acquire and rehabilitate properties and make them available to lower-income families as affordable ownership and rental housing.

Several HFAs, including Pennsylvania, Rhode Island, Colorado, and Minnesota, already have programs underway to accomplish this. Some HFAs, like Pennsylvania and Rhode Island, are modeling these programs on highly successful programs they have operated for many years to revive vacant properties and make them available as affordable housing.

A number of HFAs have contributed their own resources to these efforts, providing grants and loans to community partners and offering HFA financing to those who develop and buy these properties. Some HFAs have built incentives into their Housing Credit allocation plans to encourage developers to buy and renovate foreclosed properties and turn them into affordable rental housing with the Housing Credit.

In Ohio, we are actively exploring foreclosed property programs with our most seriously impacted local communities and anticipate using some of our own funds to support them. But, our funds and those of other HFAs are inadequate to deal with the huge scale of this problem.

Mr. Chairman, your legislation's proposed state loan and grant program would significantly strengthen and expand state HFA initiatives in this area. States are well positioned to undertake this program, as many are already engaged in the kinds of initiatives it is designed to support. We can direct these new, but limited, resources to the areas that need them most. States have strong strategic partnerships with local communities and nonprofits that will be essential to the program's success, and we can bring other resources we administer, like the Housing Credit, to bear in addressing this problem.

We offer the following comments on the program and suggestions for strengthening it.

In most cases, we expect states to lend the money to local partners and use their loan payments to repay the federal loans. Therefore, it is important that the federal loans be non-recourse and bear no interest, as the bill provides.

Based on our experience with similar programs, state HFAs believe it is important for Congress to understand that the full repayment of these loans in the short-term and even over the long-term may not always be possible. Continued home price depreciation will likely make it difficult in some cases to resell properties for what states and their partners will need to pay for them. In many cases, market conditions will make it impossible to recover necessary rehabilitation expenses.

The bill prohibits repeat lending to entities that have previously borrowed amounts under this program and repaid less than 95 percent of the amounts due under previous loans. Because of the difficulty in achieving full repayments, we believe this 95 percent threshold is too high and recommend reducing it substantially.

The chances for higher resale values further into the future after the real estate cycle rebounds is possible, although not certain. Property values in many communities may take many years to recover.

Mr. Chairman, we support the income targeting provisions in the bill. It's appropriate to focus federal assistance on families that need help the most. However, because so many middle-income families and communities are affected by today's housing crisis, broader targeting than usually applies to federal housing programs is appropriate, particularly in the homeownership area.

Broader income targeting promotes economic integration and allows for the rebuilding of communities with a similar economic mix as they enjoyed before the current downturn.

We are concerned that the bill's prohibition on purchases of homeownership properties with prices that exceed 90 percent of average area sales price will limit the program's ability to serve people that need help and stabilize economically integrated neighborhoods. We suggest that the program, at least, include all properties eligible for MRB financing, which would include properties that cost up to 110 percent of average area sales price in economically distressed targeted areas. Many areas hard hit by the subprime lending and foreclosure crisis are targeted areas and would benefit from the increased price flexibility the MRB program affords.

We are also concerned that the bill requires six months of payments before insurance endorsement for new loans with total debt-to-income ratios greater than 40 percent. Delaying endorsement for new mortgages will make it much more difficult for HFAs to include them in their bond-financed mortgage programs. We recommend you permit flexible underwriting standards without the six-month delay.

Mr. Chairman, we are also concerned that the bill's timetables for completing allocations plans, obligating and spending funds, and reselling homeownership and rental properties are unrealistically tight.

Foreclosure proceedings involve complicated legal steps that preclude rapid action. Working though complex mortgage securities, gaining clear property title control, and negotiating with owners and lenders will be time-consuming and difficult. Analyzing rehabilitation costs and working up rehabilitation plans will also take time. We recommend you lengthen the bill's deadlines to balance the need to move quickly with the time necessary to do this job properly.

Mr. Chairman, thank you again for the opportunity to testify on behalf of NCSHA. My colleagues and I stand ready to work with you to improve this bill and advance it rapidly.